Annual Report 1996

TREGO Energy Inc.

In central Niger, between the Great Sahara Desert and the grass-lands live the *Wodaabe*. They number among the last nomads in Africa, and indeed among the last nomads on earth.

At the end of the rainy season each year, the *Wodaabe* gather for a magnificent celebration they call the *Geerewal*. The young men compete in beauty at the *Geerewal*. They adorn them-selves in their fanciest costumes and paint their faces with designs such as that above.

TG World Energy Inc., a Trego subsidiary, signed an agreement to explore the Tenere Block in central Niger on March 6, 1997.

CORPORATE PROFILE

TREGO ENERGY INC. is an emerging junior oil and gas exploration and development company that has built a base of long life proven oil reserves in southeast Saskatchewan. The oil reserves are complemented with an inventory of detailed and drillable development and exploratory prospects located on company owned lands, which provides Trego continued growth in cash flow and the potential for major break through in oil and gas reserve growth.

The company is listed on the Alberta Stock Exchange and trades under the symbol "TEI".

At December 31, 1996, the Company had 11,895,738 shares issued and outstanding.

COMPANY PHILOSOPHY

- to restrict capital expenditures to southeast Alberta and southeast Saskatchewan
- core properties must be Company operated
- properties must have a significant working interest
- Company owned infrastructure
- internally generated prospects on company owned lands
- carry an inventory of exploration leases that may be farmed out or sold
- through farmout, expose the company to higher risk, but high potential prospects

TREGO Energy Inc.

NOTICE OF ANNUAL MEETING

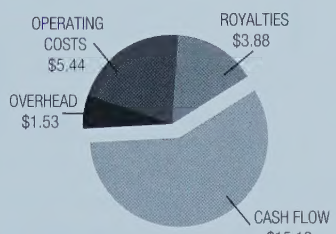
You are cordially invited to attend
the Annual General Meeting of TREGO ENERGY INC.
at 3:30 p.m., Thursday May 29, 1997
in the Cardium Room, Calgary Petroleum Club,
319 - 5th Avenue S.W., Calgary Alberta.

TABLE OF CONTENTS

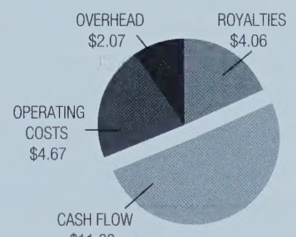
CORPORATE HIGHLIGHTS

FINANCIAL ($,000) except per share data *For Years Ending December 31,*	1996	1995	1994	1993
Gross Revenue	$ 2,678	$ 1,236	$ 375	$ 324
Cash Flow	$ 1,560	$ 624	$ 104	$ 139
per share ($)	$ 0.16	$ 0.10	$ 0.02	$ 0.03
Net Income	$ 535	$ 137	$ (49)	$ (21)
per share ($)	$ 0.05	$ 0.02	$ (0.01)	$ (0.01)
Net Capital Expenditures	$ 3,793	$ 2,744	$ 646	$ 1,421
Long Term Debt	$ 1,200	$ 800	$ –	$ 35
Shareholder Equity	$ 5,208	$ 2,223	$ 1,846	$ 1,677
Issued Shares (end of period)	11,895	7,693	6,377	5,380
Weighted Average shares	10,049	6,316	5,536	4,633
OPERATIONAL (average 94 to 98% oil production)				
Annual Production				
Gas (MCF)	27,150	31,754	12,387	10,950
Oil (bbls)	100,115	53,453	16,316	14,600
Daily Production				
Gas (MCF)	74	87	34	30
Oil (bbls)	274	146	45	40
Average BOE/D	281	155	48	43
BOE/D end of period	391	211	127	45
Pricing	$ 26.03	$ 21.83	$ 20.97	$ 20.64
Royalties ($/BOE)	$ 3.88	$ 4.06	$ 4.20	$ 1.60
Operating Costs ($/BOE)	$ 5.44	$ 4.67	$ 5.75	$ 6.39
G&A Costs ($/BOE)	$ 0.88	$ 0.86	$ 5.43	$ 3.79
Interest ($/BOE)	$ 0.65	$ 1.21	$ –	$ –
Net Back ($/BOE)	$ 15.18	$ 11.03	$ 5.59	$ 8.86

COMPANY PROFITABILITY



1996



1995

Average Price: 1996 - $26.03/bbl
1995 - $21.83/bbl

PROVEN RESERVES AND EXPLORATION LANDS	1996	1995	1994	1993
Reserves				
MMSB*	1,520	1,111	289	137
MMCF	199	318	320	300
Exploration Land Holdings (acres)				
Gross	35,552	25,835	55,345	53,920
Net	23,265	12,512	18,251	19,957
Land Values	$ 1,314	$ 904	$ 927	$ 1,123
Proven Reserves @ 15% DCF*	$ 11,606	$ 8,063	$ 3,685	$ 1,513

* @ Feb 1, 1997 - Proven Reserves were valued at $16,248,000 discounted at 15% with total proven oil reserves of 2,130.0 MSTB.

TREGO Energy Inc.

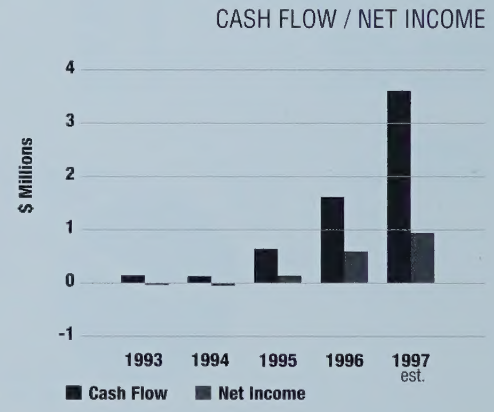
Report To Shareholders

Trego Energy Inc. is entering an exciting phase of its corporate growth. While the company directs most of its capital investment to developing and increasing its cash flow and net income in Canada, it has also initiated a plan to expose Trego to the high potential of an international oil and gas operation with limited capital exposure, and also added share value by turning its interest in ammonite leases into a visible value.

A number of significant events were accomplished in 1996. The highlights for the year include:

- *Gross revenue increased 116% to $2.68 million.*
- *Cash flow increased 115% to $1.56 million.*
- *Net income increased 290% to $.54 million.*
- *Proven reserves increased 35% to 1.54 million BOE.*
- *A Private Placement was completed in the amount of $2.4 million by issuing 4 million shares at $.60/share.*
- *The Board of Directors were restructured to accommodate the Private Placement.*
- *A plan was initiated to expose Trego to the high potential of international activity.*
- *A plan was completed wherein Trego exchanged its interest in Ammonite leases for a 34.8% interest in North American Gem Inc., a public company.*

FINANCIAL HIGHLIGHTS



During 1996, Trego remained focused on building cash flow and net income in southeast Saskatchewan. Our strategy of concentrating on a few core areas which Trego operates, with a large working interest and infrastructure in place, has worked successfully. Cash flow of $1.56 million ($.16/share) was generated from just three properties and 33 wells (net 25.6 wells). More importantly, these same properties offer considerable development potential with sufficient identified development drilling locations to satisfy Trego's drilling budget for the next two to three years. These development locations are complimented by a number of exploration prospects on Trego owned lands that will provide Trego with continued growth in cash flow, net income and the potential for major addition in oil and gas reserves.

In 1996, Trego completed a Private Placement of $2.4 million at $.60/share. The Private Placement was completed at a 28% premium to market at that time which is a reflection of the added value the investors recognized in the Company. The investment group also received 2.0 million warrants that are exercisable at $.80/share or $.90/flow through share until June 4, 1998. The expected exercise of these warrants will provide Trego with additional financing through 1997 and 1998. At the end of 1996, Trego had 11,895,738 common shares issued and outstanding.

OPERATIONAL HIGHLIGHTS

In 1996, Trego's net capital investment was $3.65 million and consisted of participating in 7 wells (4.33 net wells) resulting in 6 oil wells (3.93 net oil wells) and one dry hole (.4 well). Trego also incurred capital expenditures for upgrading oil batteries at Cantal/Alida, Steelman and Weyburn and completed a number of gathering lines to reduce operating costs which will have full impact in 1997. In 1996, 10,753 net acres were also added to the exploration land inventory of the Company.

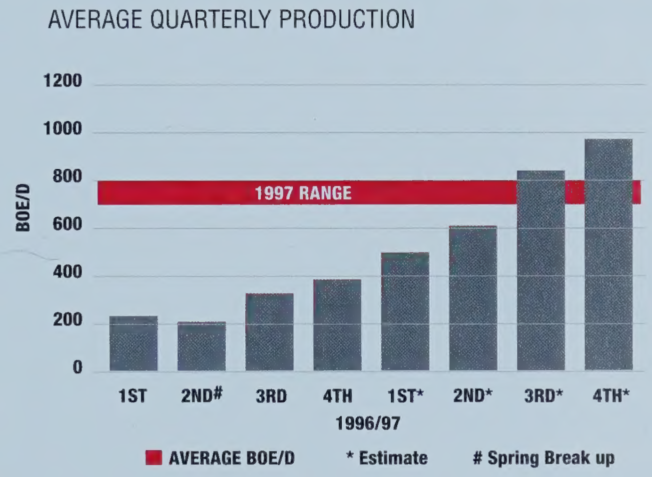
Overall in 1996, Trego added 509,700 proven barrels of oil, a 50% increase while proven gas reserves declined by 32% or 92 MMCF. At December 31, 1996, Trego had proven oil reserves of 1.52 million barrels of oil and 199 MMCF of proven gas reserves valued at $11.606 million discounted at 15%. Exploration lands now total 23,265 net acres out of 35,552 gross acres (average 65% working interest) and were independently evaluated at $1.314 million.

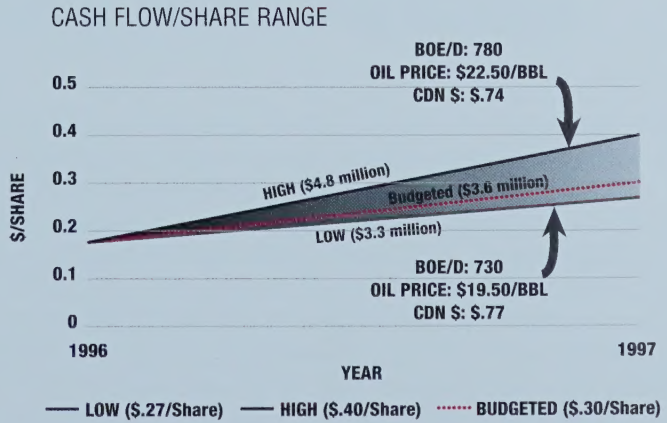
OUTLOOK

The outlook for Trego Energy Inc. is very positive. In 1997, Trego plans to concentrate on developing its properties in southeast Saskatchewan. For the year, Trego has budgeted $7.6 million, allocating of $2.2 million for property purchases and $5.4 million for exploration and development drilling and related tie-in costs, equipping and facility additions. Effective February 1, 1997, Trego acquired two private companies for $2.0 million that own joint interest with Trego in property at Weyburn. This purchase added a further 545,900 of proven oil reserves to the Company but also 100% control of most of our 1997 development drilling budget. I am pleased to report that Trego has a drilling rig under contract that becomes available to the Company immediately after spring breakup in May 1997 to commence our summer drilling program.

Management is anticipating that production for the year will average between 700 to 800 BOPD and 100 MCF/d. We anticipate exiting 1997 producing in excess of 1000 BOPD. We expect cash flow will range between $.27/share to a high of $.40/share based on different realistic parameters. For budget purposes, we have based our projections on oil prices of $20.00 WTI and a $.75 Canadian dollar, forecasting cash flow to be $3.6 million or average $.30/ share. In 1997, Trego will be attempting to add new core areas by drilling two 100% exploration wells.

Combined with increasing cash flow in Canada, Trego will add share value in 1997, without further capital or carrying costs by





being a major shareholder of a public company actively exploring on the international scene. As sales of gemstones within North American Gem Inc. grow, Trego will see share appreciation on its holdings in this public Company.

Trego is also in the fortunate position of having an efficient and dedicated staff consisting of four full time people. Since Trego has maintained its focus of few properties with a high working interest, we do not anticipate adding staff despite anticipated doubling of production and cash flow in 1997.

CORPORATE

To accommodate the completion of the Private Placement, Mr. David B. Ilsley, Mr. Kenneth Cairns, Mr. R. David Kimmitt and Mr. Stanley Prenioslo resigned from the Board of Directors. In their place, Mr. Jimmy Thorogood, Mr. Wilfrid Loucks, Mr. Clifford James and Mr. Kishore Sahkrani were appointed to the Board joining Hugh Borgland and Murray J. Berg. Mr. Wilfrid Loucks was appointed as Chairman of the Board, Mr. Stanley Prenioslo will continue in his full time capacity as Vice President of Exploration, and Mr. Ronald J. Simpson was appointed Chief Financial Officer. Mr. Loucks and Mr. Simpson act on an advisory basis and are paid only in the form of stock options in Trego. All three will have significant input into the future plans of the Company.

I wish to thank the former Board members for their valued input since the inception of the Company. I welcome the new Board members and truly believe it will be a rewarding association for all shareholders. I also welcome Mr. Robert Matson to the newly created position of Operations Manager in October 1996 and wish to thank Ms. Lisa deRegt for her efficient handling of production and financial accounting functions and office administrative responsibilities.

On behalf of the Board of Directors

Hugh D. Borgland
President and Chief Executive Officer

Wilfrid A. Loucks
Chairman of the Board

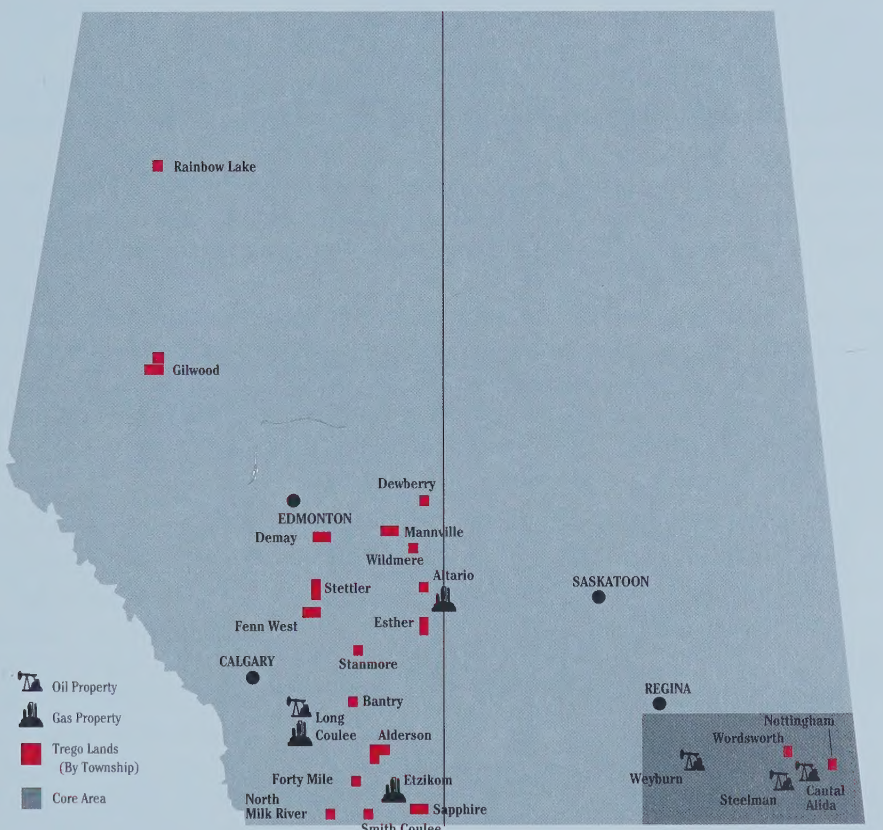
Exploration and Land

Carrying an inventory of exploration lands is a major component of Trego's exploration strategy. In 1996, the Company added 10,753 net acres of exploration leases and at December 31, 1996, Trego owned 23,265 net acres with an average interest of 65%. This compares to a 48% average interest in 25,835 gross acres and 14,356 net acres at the end of 1995. The Company has a number of identified prospects located on these lands. In 1997, Trego plans to add a further 10,000 net acres to its exploration land holdings.

Exploration Land Summary

The following value was independently assigned to Trego's undeveloped oil and gas leases at January 1, 1997:

	Acres Gross	Acres Net	Average Interest	Appraised Value
Alberta	28,960	19,269	67%	$ 440,593
Saskatchewan	6,592	3,996	61%	$ 873,507
Total	35,552	23,265	65%	$ 1,314,100



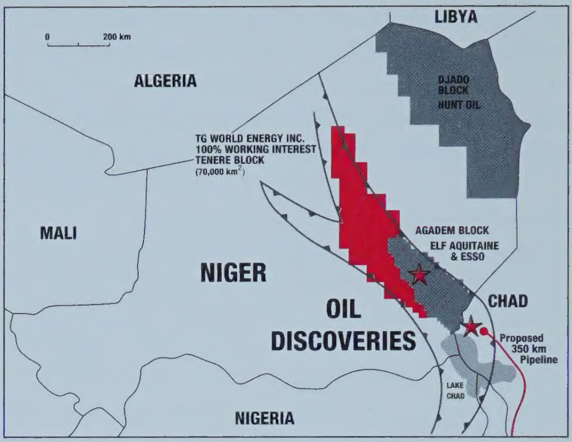
TG World Energy Inc.

In 1996, a plan was initiated for Trego Energy Inc. to be exposed to the high potential of an international oil and gas operation, without the financial risk inherent in such an operation. A private company called TG World Energy Inc. was formed of which Trego Energy Inc. owns a 40% interest.

In November 1996, TG World Energy Inc. entered into a letter of intent which was finalized in March 1997, to acquire a 70,000 square kilometer concession called the Tenere Block in Niger, Africa. This concession is part of an extensive rift system trending north from Chad where several hydrocarbon accumulations ranging from 250 to 300 million bbls of oil have occurred. The Tenere block offsets the Agadem block currently being explored by Esso and Elf Aquitaine. It is reported that there are oil and gas discoveries on four separate structures on the Agadem block. A 30 inch, 200,000 BOPD pipeline is also planned from Chad through the Cameroons to a deep water port. Once this line is completed it will have significant impact on the economics of West Africa.

TG WORLD ENERGY INC. *cont.*

A public company is currently being formed of which Trego Energy Inc. will initially own approximately 51.3%. The objective is for Trego Energy Inc. to be exposed internationally as a shareholder only, and will not have further funding requirements. The public company will raise the required capital for its operations through equity financing.



NORTH AMERICAN GEM INC.

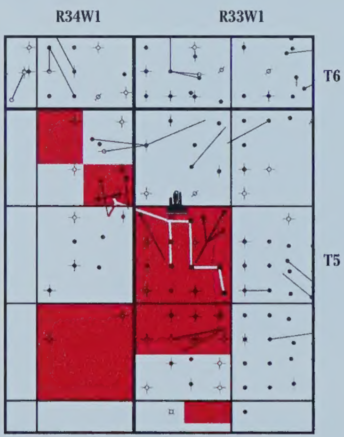
At the end of 1995, Trego owned a 50% interest in 3,689 acres of ammonite leases. Since these lands were not part of the Company's overall strategy, a plan was initiated to sell the leases to a seperate Public Company. Effective December 23, 1996, the leases were sold to North American Gem Inc. for $100,000 cash and common shares. Trego now owns 4,054,000 shares of NA GEM or 34.8% and will not be involved in this business, other than as a shareholder.

Ammonite is a fossilized extinct marine animal, the shell of which is used to produce multi-colored gemstones, commonly known as ammolite. North American Gem Inc., a publicly listed company on the Alberta Stock Exchange, is in the business of mining, manufacturing and marketing the ammolite gemstone.

DEVELOPMENT PROPERTIES

Trego Energy Inc. is well positioned for continued growth from its existing major properties. In keeping with our corporate strategy, Trego has significant interests; owns the production facilities; and its main producing properties are located in its core areas of southeast Saskatchewan. On these properties, we have identified 19 horizontal locations and 18 vertical locations. In 1997, we plan to drill 7 horizontal wells (6.25 net wells) and two 100% exploration vertical wells.

CANTAL/ALIDA AREA



83% average interest
14 producing wells (10.7 net)
100% battery w/ disposal facilities
2000 acres
Development locations
-4 horizontal
-6 vertical
1 horizontal;
1 exploratory well; (1997)

The Cantal/Alida area comprises 20% of our proven reserves and 46% of our daily production. In 1996, Trego drilled one horizontal well and drilled a leg off an existing horizontal well. Trego now operates 14 oil wells with an average interest of 81%, and a 100% owned Battery which is pipeline connected for both oil and gas sales.

In 1997, Trego has budgeted two 100% wells consisting of one horizontal well and one exploration vertical location. The horizontal well was drilled in January, 1997 resulting in a successful well producing approximately 150 BOPD, and is now tied into our Battery. The Company still has 3 horizontal and 6 vertical locations identified for drilling in subsequent years.

WEYBURN AREA

Weyburn is a major producing area for Trego and provides 78% of our proven reserves and 50% of our daily production. In 1996, Trego drilled four successful horizontal oil wells (2.3 net wells) and participated for a 25% interest in acquiring a further 240 acres in the Weyburn area. The Company also acquired a 50% interest in 3 additional oil wells in this area. Trego now owns an interest in 16 producing wells (8.3 net producing wells).

WEYBURN AREA
cont.

Prior to the end of the year, Trego reached an agreement with its partners to acquire their interest in certain producing wells and the remainder of the undeveloped lands. This purchase was closed on February 1, 1997, and increases Trego's net producing wells to 12.3 out of a total of 16. Trego now controls most of its 1997 budget.

In 1997, Trego plans to drill 6 horizontal (5.25 net wells) and drill a leg off an existing horizontal well. After completing our 1997 drilling program, Trego still has 7 horizontal locations planned for drilling in 1998.

25% to 100% working interest

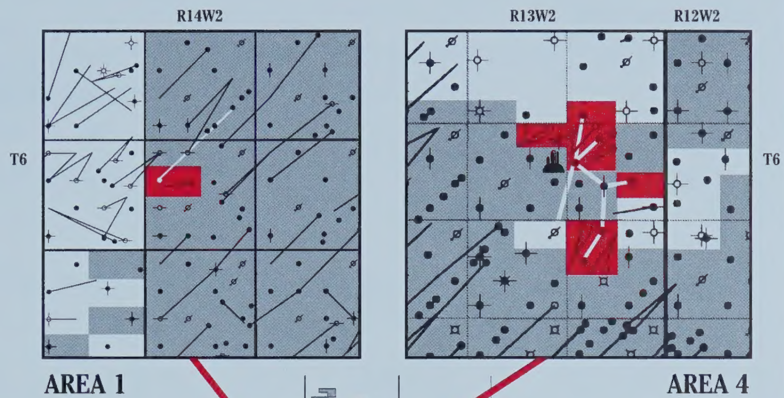
16 producing oil wells

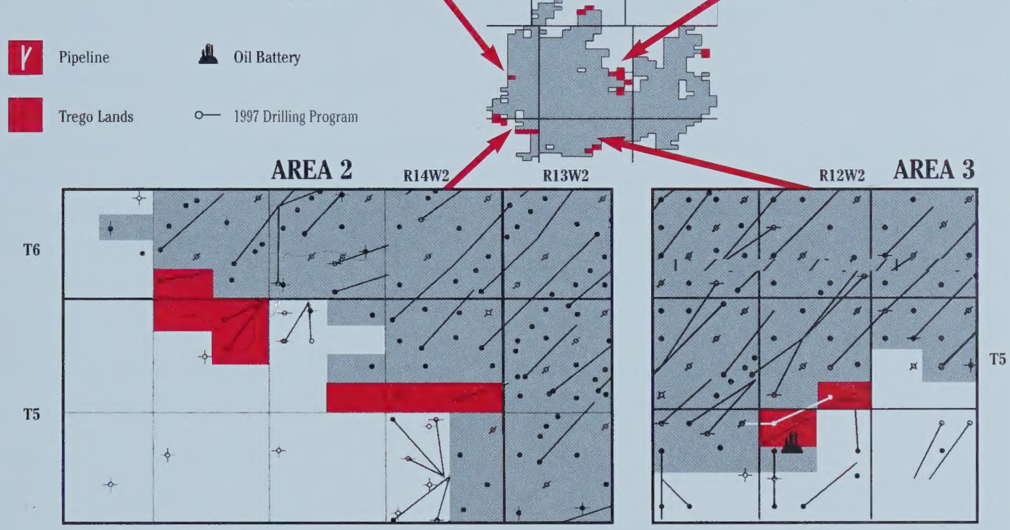
2 operated Batteries w/ disposal facilities

1680 acres

Development locations
- -13 horizontal
- -1 vertical

6 new horizontal wells;
1 new leg; (1997)





STEELMAN AREA

Steelman is an area that offers Trego considerable future potential. The Company currently has 3 producing wells that are pipeline connected to a Battery and water disposal well which is 63% owned by Trego. In 1996, Trego tested a geological concept by drilling a well resulting in a successful oil well producing 30 BOPD with a 37% water cut. This well is now tied into our Battery to reduce operating costs.

In 1997, Trego plans to shoot a detailed 3-D seismic program to identify a further 6 to 10 locations on this property for drilling in 1998. The 3-D program will also give Trego information on the potentially perspective deep rights.

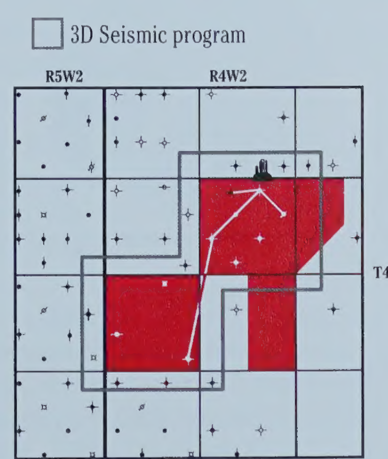
63% interest

3 producing oil wells

Battery w/ disposal facilities

1840 acres

development locations
- -1 horizontal
- -6 vertical



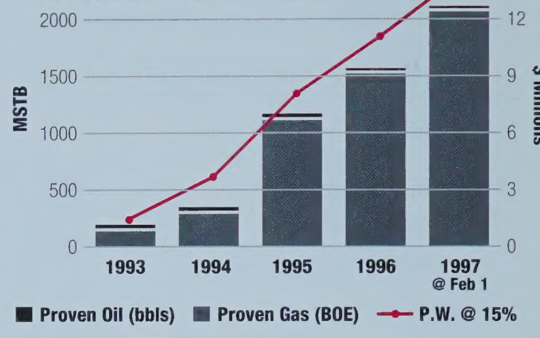
TREGO Energy Inc.

RESERVE OVERVIEW

RESERVE DISCUSSION

Sproule Associates Limited has evaluated the Company's reserves since inception to develop and maintain a consistency in reserves and value. At January 1, 1997, Sproule assigned the following value to the Company's proven reserves net of abandonment costs.

PROVEN RESERVES VS PRESENT WORTH VALUE



RESERVE SUMMARY

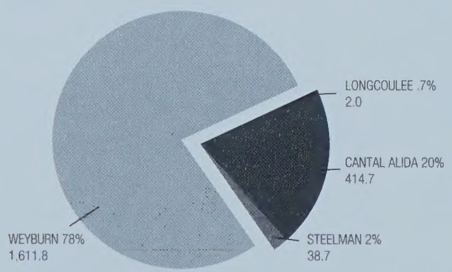
	OIL	GAS	DISCOUNTED @ 0%	10%	15%	20%
	MSTB	MMCF	$M	$M	$M	$M
CLASSIFICATION						
PROVEN PRODUCING	1,089.9	199.0	$ 20,064	11,011	9,043	7,732
PROVEN NON-PRODUCING	429.7	–	$ 5,124	3,180	2,563	2,087
TOTAL PROVEN RESERVES	1,519.6	199.0	$ 25,188	14,191	11,606	9,819

Effective February 1, 1997, Trego acquired two private companies. The sole asset, other than working capital consists of a 50% interest in Weyburn properties in which Trego already owns a 50% interest. In addition, Trego drilled a successful horizontal oil well in Janauary, 1997. Effective February 1, 1997, Sproule Associates has now increased the Company's proven reserves to 2.13 million bbls of oil, and 297 MMCF of gas reserves; with a present worth value of $16.248 million discounted at 15%.

RECONCILIATION OF RESERVES

In 1996, Trego recorded a 37% increase in proven oil reserves and a 37% reduction in proven gas reserves. The reserve additions were on our core properties in southeast Saskatchewan.

PROVEN RESERVES



PROVEN RESERVES BY AREA (MSTB)

	PROVEN OIL (MSTB)	PROVEN GAS (MMCF)
January 1, 1996	1110.5	318.0
Production Purchases		
Weyburn	29.0	
Drilling		
Weyburn	516.0	
Steelman	25.4	
Revisions		
Cantal	(38.0)	(45.3)
Weyburn	(22.7)	
Long Coulee		(46.7)
1996 Production	(100.6)	(27.0)
Total Reserves @ January 1, 1997	1,519.6	199.0

RESERVE LIFE INDEX

Based on 1996 production of 102,813 BOE, the reserve life index of the Company's proven reserves is 14.9 years. The Company only evaluates proven reserves and does not include probable.

MANAGEMENT DISCUSSION & ANALYSIS

The following discussion and analysis is management's review of the operations, financial position and outlook of Trego Energy Inc. and should be read in conjunction with audited financial statements of the Company for the years ended December 31, 1996 and 1995.

The following analysis is presented on a barrels of oil equivalent basis. Natural gas volumes are converted at a ratio of 10,000 cubic feet of gas for each barrel of oil. Gas production and pricing will have minimal effect on our BOE since 97% of the Company's production is from oil.

OVERVIEW

Trego continued to achieve growth in gross revenue, cash flow and net income. The following table summarizes our income with a conversion to performance on a barrels of equivalent basis:

	1996		1995		%
	($Thousands)	($Per BOE)	($Thousands)	($Per BOE)	Change/BOE
Oil and Gas Revenue	2,677	26.03	1,236	21.83	+19
Royalties	399	3.88	230	4.06	- 4
	2,278	22.15	1,006	17.77	+25
Administration net of overhead recovery	91	.88	48	.85	+ 3
Interest	67	.65	69	1.21	- 46
Operating	560	5.44	265	4.68	+16
Cash Flow	1,560	15.18	624	11.03	+38
Depletion & Depreciation	633	6.17	303	5.35	+15
Income before taxes	927	9.01	321	5.67	+59
Deferred income taxes	391	3.80	185	3.27	+16
Net Income for the year	536	5.21	136	2.40	+117

GROSS REVENUE

Gross revenue was $2,676,779 on the sale of 102,813 barrels of equivalent oil at an average price of $26.03/bbl. This gross revenue represents a 116% increase over 1995 and is due to an 82% increase in production and a 19% increase in oil price. Trego's production consists of 97% oil and 3% gas. The gas production is primarily solution gas produced with the oil at Cantal/Alida in southeast Saskatchewan. Production for 1996 averaged 281 BOED compared to 155 BOED in 1995. Most of this increase was from successful drilling in the Weyburn area.

ROYALTY EXPENSE

Royalty expense, including crown, freehold, and overriding royalty holders, amounted to $399,519 or $3.88/BOED in 1996. This compares to $4.06/BOED in 1995. The reduction on a per BOE basis is due to increased production from horizontal wells which is subject to incentive crown royalties in the early stages of its production life. In 1997, Trego is budgeting royalties to equate to $3.00/BOE.

OPERATING EXPENSE

In 1996, operating expenses were $559,693 or $5.44/BOE compared to $4.68/BOED in 1995. The increase was due to unexpected operating adjustments in 1996 from the purchase of the Weyburn properties. Delays in constructing gathering lines for newly drilled wells, due to a shortage of contractors, also contributed to higher operating costs. As production per well increases and improvements to facilities are completed, Trego is forecasting operating costs to reduce to $4.79/BOE in 1997.

FIELD NET BACKS

Trego achieved a field net back per barrel of $16.71/BOE in 1996 compared to $13.09/BOE in 1995, an increase of 28%. This increase is entirely due to the increase in the price of oil in 1996.

		1996		1995
Average Price/BOE	$	26.03	$	21.83
Less Expenses				
Royalty		3.88		4.06
Operating		5.44		4.68
Field Net Back	$	16.71	$	13.09
Percentage of Gross Sales		64%		60%

ADMINISTRATIVE EXPENSE

Administrative expense for 1996 was $90,688 or $.88/BOE compared to $.85/BOE in 1995. This expense is net of overhead recovery in the amount of $149,534 that is generated because Trego operates much of its joint venture property. A further $120,307 was capitalized compared to $114,000 in 1995. The Company's administrative expense prior to recovery of overhead and capitalized G & A was $360,529 in 1996, compared to $268,045 in 1995. Trego will have 100% working interest in the majority of its 1997 capital budget so that production is forecasted to increase without a substantial increase in administration costs in 1997.

INTEREST EXPENSE

Interest expense in 1996 was $ 66,609 or $.65/BOE compared to $68,736 or $1.21/BOE in 1995. Interest rate was reduced to .5% over prime rate in 1996. At December 31, 1996, Trego's long-term debt was $1.2 million.

DEPLETION & DEPRECIATION

Depletion and depreciation is a measure of the efficiency at which the Company is finding reserves and placing these reserves on stream, along with the quality of such reserves. In 1996 depletion and depreciation was $633,586 or $6.17/BOE compared to $5.35/BOE in 1995. This increase is primarily due to increased production and newly drilled production with limited production history resulting in conservative reserve estimates. Industry average for 1995 was $6.57/BOE based on a survey by Price Waterhouse.

CASH FLOW & NET EARNINGS

Cash flow was $1,560,270 in 1996 compared to $624,731 in 1995. This increase in cash flow was a result of higher product price and increased production. Cash flow on a unit basis was $15.18/BOE in 1996 compared to $11.03/BOE in 1995. This increase is primarily due to the increase in the price of oil. Cash flow per share was $.16 based on weighted average issued shares in 1996 of 10,049,130. In 1995, cash flow was $.10/share based on weighted average issued shares of 6,315,674. Net income for 1996 was $535,604 ($.05/share) compared to $136,652 ($.02/share) in 1995.

CAPITAL EXPENDITURES

Net capital expenditures in 1996 were $3,639,352 compared to $2,743,929 in 1995. The following table provides a summary of capital expenditures:

		1996		1995
Property acquisition	$	427,400	$	930,082
Geological and geophysical		164,845		225,653
Drilling and completion		2,549,097		930,822
Plant and well equipment		592,684		733,374
Other		58,483		–
Disposal of capital assets		(153,157)		(76,743)
Net capital expenditures	$	3,639,352	$	2,743,188

The 1996 capital expenditures were financed by a private placement of $2.4 million and the balance by cash flow.

INCOME TAXES

Provision for deferred income taxes increased to $ 391,080 due to the increased profitability of the Company. At December 31, 1996, the Company had various tax pools that totalled $ 4,697,714 to shelter future income. Cash taxes are not expected to be paid in 1997.

BANK DEBT & WORKING CAPITAL DEFICIENCY

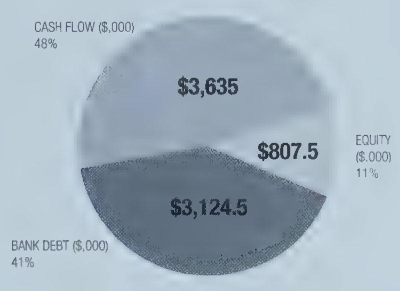
At December 31, 1996, Trego had a bank debt of $1.2 million and a working capital deficiency of $745,709 for a total obligation of $1,945,709. The Company's current line of credit is $4.0 million and bears interest at the rate of .5% over prime rate. The Company normally runs a working capital deficiency to reduce borrowing costs. The Company has increased its line of credit to $5.0 million effective April 1, 1997 to meet its 1997 budget requirements.

For 1997, Trego has budgeted capital expenditures of $7.6 million which will be financed from cash flow of $3.6 million, equity of $.8 million from the flow through portion of outstanding warrants, and bank debt of $3.2 million. It is estimated that our debt will be $4.4 million at the end of 1997 with a working capital deficiency of $.6 million for a total obligation of $5.0 million.

Based on a total debt of $5.0 million, and anticipated cash flow of $3.6 million, the debt to cash flow is 1.4 years or 11 months of annualized December, 1997 cash flow.

The majority of Trego's 1997 capital budget is on lands 100% owned by the Company without firm commitments. If oil prices fall, production does not meet expectations, or should interest rates increase significantly, Trego is in a position to stop capital expenditures immediately, hence not impairing the financial viability of the Company.

SOURCE OF BUDGET FINANCING

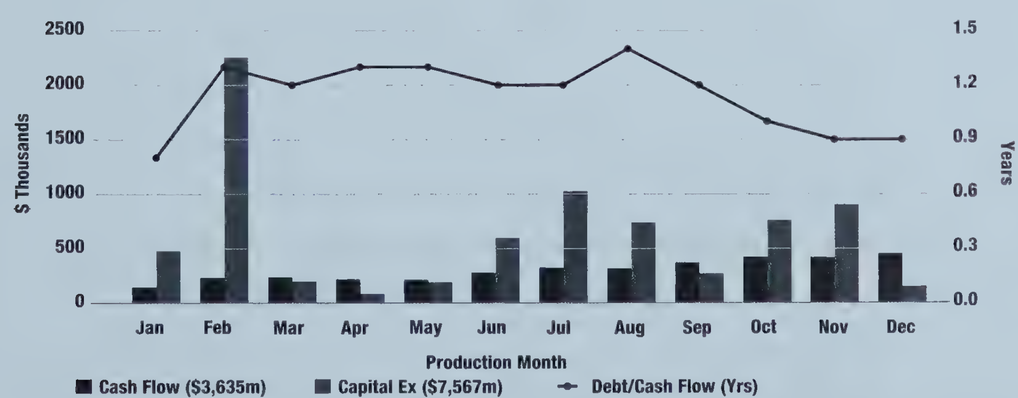


FINDING COSTS

Trego only evaluates proven reserves and does not include probable reserves in its finding costs. The calculation is on an invested capital basis, so that it reflects all costs of identifying, finding, equipping and placing the reserves on production:

	1996	1995
Shareholder Equity	$ 4,633,397	$ 2,177,465
Retained Earnings	574,782	45,622
Bank Debt	1,200,000	800,000
Working Capital Deficiency	724,709	1,400,050
Invested Capital	$ 7,132,888	$ 4,423,137
Future Investment	1,974,000	1,530,000
Total Investment	$ 9,106,888	$ 5,953,137
Proven Reserves (BOE)	1,539,900	1,135,200
Finding Cost per BOE	$ 5.91	$ 5.24

MONTHLY BUDGET



BUSINESS RISK & OUTLOOK

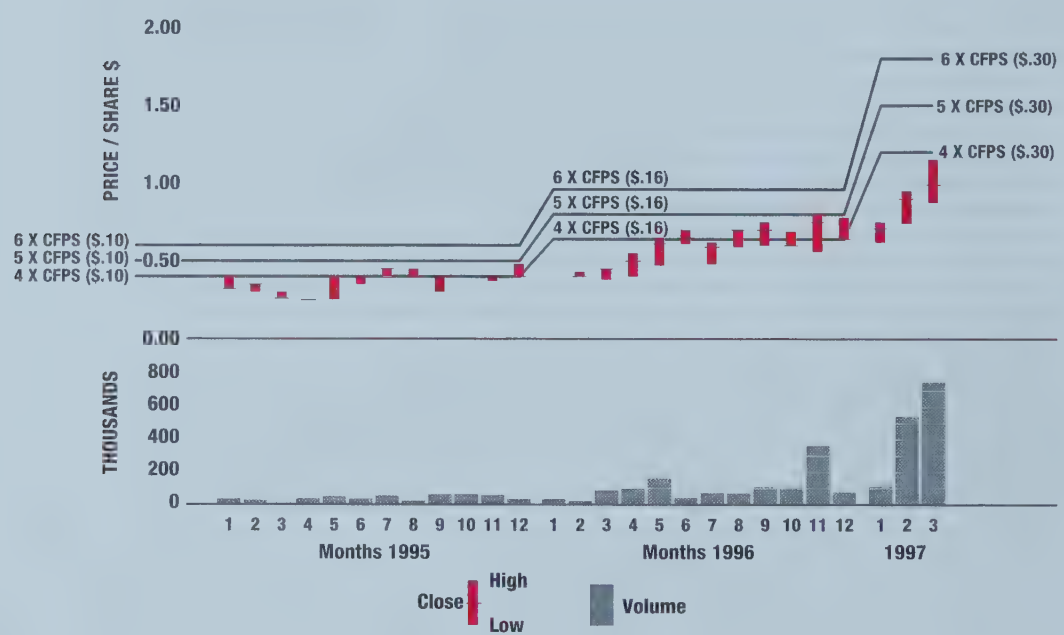
Projected cash flow from operations is dependent upon a number of factors, not all within the control of the Company. The majority of capital expenditures in 1997 will be incurred on a development program in the Weyburn area. The majority of Trego's production is oil, making the Company's cash flow sensitive to oil price. The following table sets out sensitivities to various fluctuations in risk factors in the industry.

1997 CASH FLOW SENSITIVITIES

	$M	$/Share
Oil price changes ($1.00/bbl US)	319	.026
Oil production volume changes (100 bbl/day)	544	.045
Changes in interest rate (1%)	40	.003
Changes in exchange rate (CDN. $.01)	84	.007

Trego's 1997 budget is based on crude oil price of $20.00 per bbl WTI, an exchange rate of $.75 CDN/US, an interest rate of 6%, and 1997 production of 730 BOED. The forcasted cash flow per share in 1997 is $.30/share.

SHARE PRICE VS CASH FLOW PER SHARE (CFPS)



AUDITORS' REPORT

To the Shareholders of Trego Energy Inc.:

We have audited the balance sheets of Trego Energy Inc. as at December 31, 1996, and December 31, 1995 and the statements of operations and retained earnings and changes in financial position for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1996 and December 31, 1995 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles.

Garrett Beaver

Chartered Accountants
Calgary, Alberta

BALANCE SHEET

As at December 31

Assets	1996	1995
Current assets:		
Cash	$ 6,390	$ 13,115
Accounts receivable	776,740	445,239
Promissory note (Note 3(b))	93,750	–
Prepaid expenses	47,256	–
	924,136	458,354
Capital assets (Note 2)	7,712,750	4,673,097
Investments (Note 3(a))	318,765	–
	$ 8,955,651	$ 5,131,451

Liabilities and Shareholders' Equity		
Current liability:		
Accounts payable	$ 1,669,845	$ 1,858,404
Long term debt (Note 4)	1,200,000	800,000
Deferred income taxes	796,231	202,451
Reclamation costs	81,396	47,509
Shareholders' equity:		
Share capital (Note 5)	4,633,397	2,177,465
Retained earnings	574,782	45,622
	5,208,179	2,223,087
	$ 8,955,651	$ 5,131,451

Approved by the Board:

Director:

Director:

STATEMENT OF OPERATIONS & RETAINED EARNINGS

For the Year Ended December 31	1996	1995
Revenue		
Oil and gas	$ 2,676,779	$ 1,236,029
Royalties	(399,519)	(229,793)
	2,277,260	1,006,236
Expenses:		
Administration, net of overhead recovery of $149,534 (1995 - $105,846)	90,688	48,199
Depletion and depreciation	633,586	303,113
Interest on long term debt	66,609	68,739
Operating	559,693	264,567
	1,350,576	684,618
Income before provision for income taxes	926,684	321,618
Provision for income taxes - deferred (Note 6)	391,080	184,966
Net income for the year	535,604	136,652
Retained earnings (deficit) at beginning of year	45,622	(70,095)
	581,226	66,557
Redemption and cancellation of shares (Note 5(c))	6,444	20,935
Retained earnings at end of year	$ 574,782	$ 45,622
Earnings per share	$ 0.05	$ 0.02

STATEMENT OF CHANGES IN FINANCIAL POSITION

For the Year Ending December 31	1996	1995
Operating activities:		
Net income for the year	$ 535,604	$ 136,652
Add: Items not requiring a current outlay of cash -		
Deferred income taxes	391,080	184,966
Depletion and depreciation	633,586	303,113
Cash flow from operations	1,560,270	624,731
Decrease (increase) in non-cash working capital	(567,316)	723,438
Cash provided by operating activities	992,954	1,348,169
Investing activities:		
Investment in capital assets	(3,792,509)	(2,820,672)
Proceeds on disposal of capital assets	153,157	76,743
Increase in investments and advances	(189,915)	–
Cash used in investing activities	(3,829,267)	(2,743,929)
Financing activities:		
Proceeds from long term debt	400,000	800,000
Proceeds on issuance of common shares	2,491,500	620,000
Redemption and cancellation of common shares	(17,058)	(90,689)
Share issue costs	(44,854)	(24,300)
Cash provided by financing activities	2,829,588	1,305,011
Decrease in cash	(6,725)	(90,749)
Cash, beginning of year	13,115	103,864
Cash, end of year	$ 6,390	$ 13,115
Cash flow per share*	$ 0.16	$ 0.10

* Cash flow per share is based upon cash flow from operations divided by the weighted average number of shares outstanding during the year.

NOTES TO FINANCIAL STATEMENTS
December 31, 1996

1. Summary of significant accounting policies:

Exploration and development costs -
The Company follows the full cost method of accounting for exploration and development expenditures whereby all costs directly related to the exploration for and development of petroleum and natural gas reserves are capitalized. All expenditures accumulated are depleted using the composite unit of production method based on estimated proven reserves as determined by independent petroleum engineers. Gas volumes are converted to equivalent oil volumes based upon the ratio of ten thousand cubic feet of gas to one barrel of oil. No gains or losses are recognized upon the disposition of petroleum and natural gas properties unless such treatment alters the depletion rate by more than 20%.

Oil and gas properties are subject to a ceiling test under which their carrying value, net of deferred income taxes and accumulated provision for reclamation costs, is limited to the undiscounted future net revenue from production of estimated proven oil and gas reserves, based on average prices for the year (Oil-$26.03/bbl; Gas-$1.30/mcf) plus the unimpaired costs of non-producing properties less estimated future administration, financing, reclamation costs and income taxes.

Reclamation costs -
Reclamation costs are accrued based on estimates made by independent petroleum engineers and are charged against earnings as depletion expense, using the composite unit of production method.

Flow through shares -
The resource expenditure deductions for income tax purposes related to exploratory and development activities funded by flow through share arrangements are renounced to investors in accordance with income tax legislation. Petroleum and natural gas assets and share capital are reduced by the estimated cost of the renounced tax deductions when the shares are issued.

Joint venture accounting -
A substantial part of the Company's operations are carried out through joint ventures. The financial statements reflect only the Company's proportionate interest in such activities.

Investments -
Investments over which the Company has significant influence but does not control are accounted for using the equity method. Where neither significant influence nor control exist, the investment is carried at cost. Where the investment is considered to be short term, it is carried at the lower of cost and market. Where permanent impairment in the value of the investment exists, the investment is written down to its estimated net realizable value.

2. Capital assets:

		1996		1995
Petroleum and natural gas assets (Note 4)	$	8,749,084	$	5,150,648
Furniture and fixtures		80,267		26,679
Other property (Note 3(a)(i))		–		12,672
		8,829,351		5,189,999
Accumulated depreciation and depletion		(1,116,601)		(516,902)
Net book value	$	7,712,750	$	4,673,097

Costs associated with unproved properties excluded from costs subject to depletion for the year amounted to $1,431,772 (1995 - $1,121,672).
The Company capitalized general and administrative expenses of $120,307 (1995 - $114,000).

3. Investments and promissory note:

		1996		1995
(a) Investments				
North American Gem Inc. ("N.A.G.") (i)				
4,054,667 common shares, representing 34.8% of the issued and outstanding common shares	$	278,757		–
Trego International Inc. ("T.I.I.") (ii)				
400,000 common shares, representing 11.4% of the issued and outstanding common shares		40,000		–
T.G. World Energy Inc. ("T.G. World") (ii)				
170 common shares, representing 40.5% of the issued and outstanding common shares		8		–
	$	318,765	$	–

(i) During the year, Trego Energy Inc. sold certain assets (Note 2, other property) to N.A.G. for a total consideration of $1,166,400, including cash of $100,000 and 3,554,667 shares of N.A.G., valued at $0.30 per share. The net cost of the assets sold after applying the cash received ($31,157), has been added to the cost of the original investment ($25,000). Deferred taxes resulting from this transaction of $222,600 have also been added to the cost of the investment. No gain has been reflected in these financial statements. The investment in N.A.G. is accounted for on the equity basis. The company is in the pre-production stage of operations and, as such, there were no earnings from operations for the period ended December 31, 1996. The market value per share was $0.15 ($608,200) at December 31, 1996.

(ii) The invesments in T.I.I. and T.G. World are accounted for on the equity basis. At December 31, 1996, the companies had not commenced active business operations and, as such, there were no earnings for the period ended December 31, 1996.

(b) Promissory note
The promissory note, from T.G. World Energy Inc., bears interest at prime plus 1%, is unsecured and due October 31, 1997. The Company and T.G. World Energy Inc. are considered to be related parties as a result of common ownership and directors.

4. Long term debt:

The bank loan bears interest at prime plus .50% and is secured by a General Security Agreement covering all present and acquired property and a fixed and floating charge debenture on the Company's petroleum and natural gas assets. The existing facility does not require principal repayments in the next fiscal year.

Subsequent to year end, the Company increased its credit facility to $4,000,000 to assist in the financing of certain oil and gas acquisitions (Note 8). The increased facility bears interest at prime plus .50%. Principal repayments (40 at $100,000) are scheduled to commence July 1, 1997.

5. Share capital:

Authorized share capital consists of an unlimited number of common and preferred shares. The following summarizes the movement in the common share account during the year:

	Number of shares	
	1996	1995
Opening balance	7,693,238	6,377,238
Issued for cash (Note 5(d))	4,000,000	1,550,000
Options exercised	240,000	–
Redeemed and cancelled	(37,500)	(234,000)
	11,895,738	7,693,238

	Amount	
	1996	1995
Opening balance	$ 2,177,465	$ 1,915,652
Issued for cash, net (Note 5(d))	2,400,000	345,092
Options exercised	91,500	–
Redeemed and cancelled	(10,614)	(69,754)
Share issue costs, net of deferred income taxes	(24,954)	(13,525)
	$ 4,633,397	$ 2,177,465

b) In 1995, the Company issued 1,550,000 flow through shares for total cash consideration of $620,000. In accordance with the Company's accounting policy, the resulting income tax effects of $274,908 were applied to reduce the Company's petroleum and natural gas assets.

c) Pursuant to a Normal Course Issuer Bid, the Company redeemed and cancelled 37,500 shares (1995 - 234,000) at a cost of $17,058 (1995 - $90,689), an amount in excess of the average cost of the shares by $6,444 (1995 - $20,935). The excess amount has been charged to retained earnings in the year.

d) Shares issued during the year (4,000,000 at $0.60) included warrants which entitle the holders to acquire up to 2,000,000 common shares at $0.80 or 2,000,000 flow through common shares at $0.90. These warrants are exercisable prior to June 3, 1998.

e) As at December 31, 1996, there were 192,000 common shares held in escrow (1995 - 489,000).

f) Stock options have been granted to directors, employees and consultants as follows:

Expiry Date	Number	Price
June 30, 1998	210,000	$0.50
September 15, 1999	170,000	$0.40
June 4, 2001	680,000	$0.50
October 15, 2001	75,000	$0.50
	1,135,000	

Subsequent to year end, 50,000 options were exercised for a total consideration of $20,000.

6. Income taxes:

The income tax provision on the income statement differs from the expected income tax provision as follows:

	1996	1995
Expected income taxes	$ 410,898	$ 142,605
Add (deduct) effects of:		
Non deductible crown royalties	124,001	85,419
Non deductible depletion and depreciation	38,025	31,149
Resource allowance	(178,813)	(76,021)
Other	(3,031)	1,814
Actual income taxes	$ 391,080	$ 184,966

7. Related party transactions:

Companies controlled by certain directors of the Company are participants in various oil and gas joint ventures with Trego Energy Inc. These financial statements include normal account balances with these companies as a result of the joint participation in these ventures.

8. Subsequent event:

Subsequent to year end, the Company acquired 100% interest in two companies for a total cash consideration of $2,039,540, after an adjustment for net working capital of $39,540. These companies are currently being wound up into Trego Energy Inc.

The acquired companies' sole assets, other than working capital, consist of a 50% interest in petroleum and natural gas properties in which Trego Energy Inc. already owns the other 50% interest.

9. Financial instruments:

The Company's financial instruments that are included in the balance sheet are comprised of accounts receivable, current liability and long-term debt.

(a) Fair values of financial assets and liabilities

The fair values of financial instruments that are included in the balance sheet, including long-term debt, approximate their carrying amount due to the short-term maturity of those instruments and the floating prime rate applied to long-term debt.

(b) Credit risk

Virtually all of the Company's accounts receivable are with customers in the oil and gas industry and are subject to normal industry credit risks.

(c) Interest rate risk

At December 31, 1996, the increase or decrease in net earnings for each one percent change in interest rates on floating rate debt at December 31, 1996 amounts to $6,600.

Corporate Summary

DIRECTORS

WILFRID A. LOUCKS,
Chairman of the Board, Calgary, Alberta

HUGH D. BORGLAND,
President and CEO, Calgary, Alberta

CLIFFORD M JAMES,
Calgary, Alberta

MURRAY J. BERG,
Calgary, Alberta

JIMMY L. THOROGOOD,
Calgary, Alberta

KISHORE SAKHRANI,
Central, Hong Kong

OFFICERS & KEY PERSONNEL

WILFRID A. LOUCKS,
Chairman of the Board

HUGH D. BORGLAND,
President and CEO

STANLEY M. PRENIOSLO,
Vice President, Exploration

RONALD W. SIMPSON,
Chief Financial Officer

ROBERT MATSON,
Operations Manager

LISA de REGT,
Accountant and Administration

TREGO Energy Inc.

SOLICITORS
Burstall Ward
Calgary, Alberta

AUDITORS
Garrett Power, Chartered Accountants
Calgary, Alberta

BANK
Canadian Western Bank
Calgary, Alberta

TRANSFER AGENT
Montreal Trust
Calgary, Alberta

LISTING INFORMATION
Alberta Stock Exchange
Symbol: "TEI"
Outstanding shares: 11,895,738

Designed & Produced by
The Gold Group Inc.
Calgary, Alberta, Canada

780, 700 - 4th Avenue S.W.,

Calgary, Alberta T2P 3J4

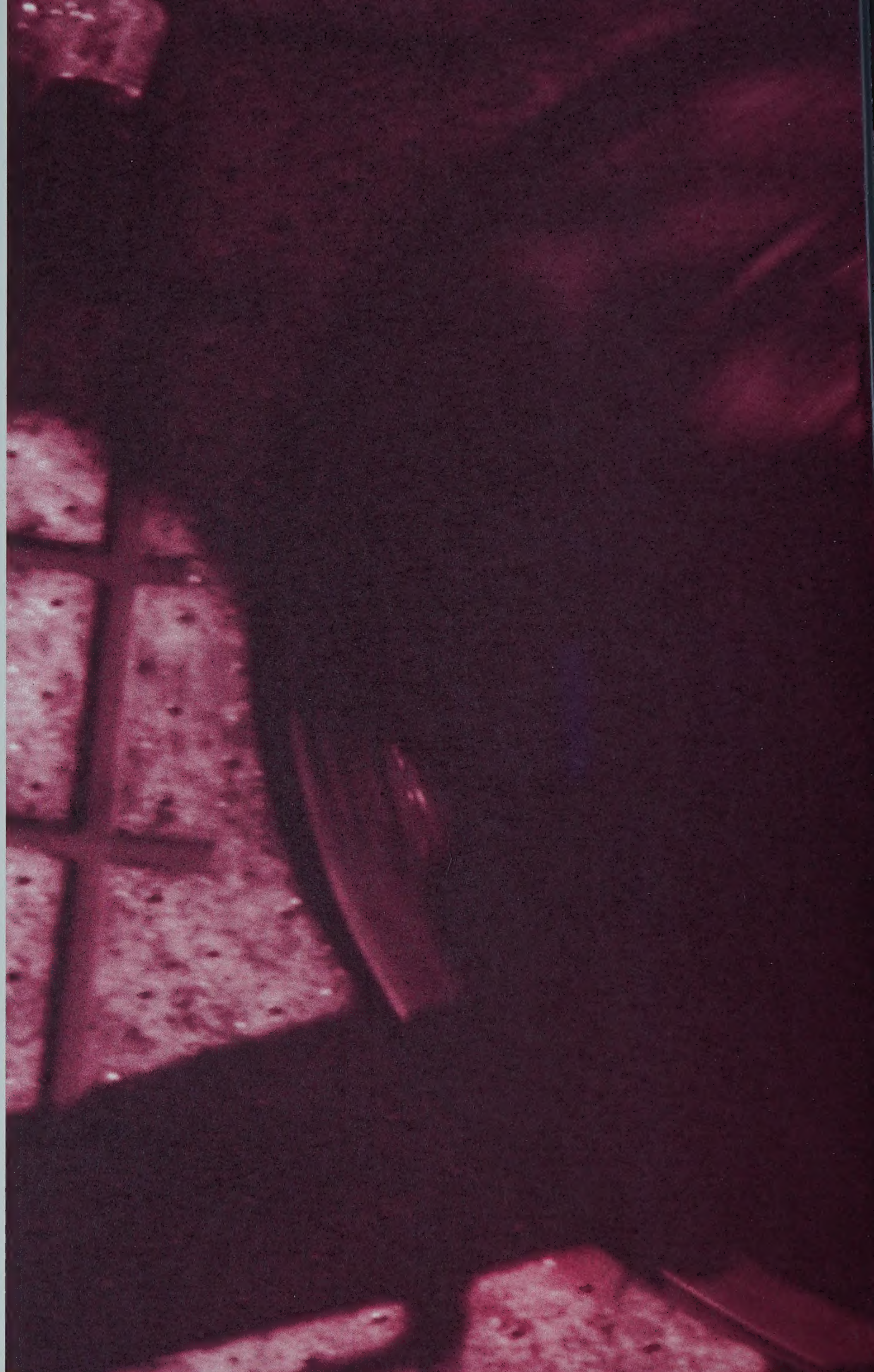
Phone: (403) 266-8090

Fax: (403) 266-8094

e-mail: tregoenergy@msn.com

website: www.tregoenergy.com

Trading Symbol: TEI on ASE



TREGO Energy Inc.

Annual Report 1996